Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Amendment of the Commission's Rules: Regulatory Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers	)	RM 9210
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	
Transport Rate Structure and Pricing	)	CC Docket No. 91-213
	)	
End User Common Line Charge	)	CC Docket No. 95-72

REPLY COMMENTS OF TIME WARNER COMMUNICATIONS HOLDINGS INC.

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ATTORNEYS FOR TIME WARNER COMMUNICATIONS HOLDINGS INC.

February 17, 1998

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REPLY COMMENTS OF TIME WARNER COMMUNICATIONS HOLDINGS INC.

Time Warner Communications Holdings Inc. ("TWComm"), by its attorneys, hereby submits its reply comments in opposition to the CFA Petition.[1]

DISCUSSION

In the Access Charge Order, the FCC established the framework for reforming interstate access charges. Most importantly, the Commission revised the interstate access rate structure so that incumbent LECs will generally recover the costs of access in the manner in which they incur them. This reform reduces the distortions, such as those in the Commission's tandem

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[1] See Petition for Rulemaking ("CFA Petition") filed by the Consumer Federation of America, the International Communications Association, and the National Retail Federation ("petitioners") on December 9, 1997.

switching and tandem-switched transport rates, that have stunted the development of access competition. Thus, services such as tandem switching and tandem-switched transport should soon become subject to competition for the first time.

The FCC also adopted a combination market-based, prescriptive approach to lowering access charges. The Commission decided to rely initially on market forces to lower interstate access charges, although it acknowledged that such competition would take time to develop. In the event that competition failed to develop in particular markets, the Commission required incumbent LECs to submit cost studies no later than February 8, 2001 for interstate access services not subject to competition.[2] In the meantime, the rate at which incumbents must lower their interstate access rates per year to reflect productivity gains (the so-called X-Factor) was increased.

The petitioners argue that it is now clear that the FCC overestimated the likelihood that interstate access competition will develop. They argue that the success of the market-based approach depends on the availability of network elements. UNE competition will not develop, they assert, because of a combination of ILEC resistance tactics and the Eighth Circuit's decisions in the Iowa Utils. Bd. v. FCC case. Based on this prediction, they urge the Commission to abandon its market-based approach and begin a proceeding for determining cost-based access

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[2] See Access Charge Reform, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, First Report and Order at ¶ 267 (rel. May 16, 1997) ("Access Charge Order")

charge levels three years earlier than the Commission had originally proposed.

This request is simply the most recent of many requests by the petitioners and the supporting commenters that the FCC lower access charges immediately. The arguments in favor of this approach are no more convincing now than when the Commission rejected them less than a year ago.

First, it is too early to tell whether the Eighth Circuit decisions in Iowa Utils. Bd. v. FCC (overturning the FCC's pricing and "pick and choose" rules and holding that ILECs are not required to provide elements on a combined basis even if they are already combined in the ILEC network)[3] will prevent significant UNE entry. It is true that the uncertainty surrounding the terms and conditions under which UNEs will be provided has slowed the introduction of access via UNEs.[4] However, state regulators are fully capable of devising rules that permit the development of UNE access competition without requiring ILECs to offer existing combinations of UNEs in

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[3] See 120 F.3d 753 (8th Cir. 1997) (incorporating the original July 18th and the subsequent October 14th decisions).

[4] It is important to note, however, that the Eighth Circuit had stayed the UNE pricing rules adopted by the FCC in the Local Competition First Report and Order long before the FCC adopted the Access Charge Order in May of 1997. See Iowa Utils. Bd. v. FCC, 109 F.3d 418 (8th Cir. 1996). Notwithstanding the fact that it could not count on forward-looking prices for UNEs, the FCC still adopted a market-based approach to lowering interstate access rates. AT&T's attempt to characterize the rules governing the provisioning and pricing of UNEs as settled at the time of the access charge proceeding, see AT&T Comments at 5, 12, is therefore misleading.

violation of the Eighth Circuit's rulings. Indeed, this issue should ultimately boil down to the level of so-called "glue" charges ILECs may impose on requesting carriers seeking to recombine UNEs. Petitioners have not demonstrated that such charges will not permit UNE-based competition.

Second, in the Access Charge Order, the Commission did not rely exclusively on the availability of UNEs as the basis for the development of access competition. On the contrary, the Commission relied upon the availability of UNEs *as well as* the entry of facilities-based competitors relying on cost-based interconnection.[5] Moreover, the logic of the FCC's adoption of a market-based approach to access charge reform demonstrates that the Commission envisioned facilities-based competition as the more important of the two modes of entry for reforming access charges. For example, the central advantage cited by the Commission of market-based approach over prescription was as follows:

> Competitive markets are superior mechanisms for protecting consumers by ensuring that goods and services are provided to consumers in the most efficient manner possible and at prices that reflect the cost of production. . . . In addition, using a market-based approach should minimize the potential that regulation will create and maintain distortions in

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[5] See Access Charge Order at ¶ 262. As the Commission made clear in the Local Competition First Report and Order, interconnection refers to the exchange of traffic between competing local carriers and is distinct from access to UNEs. See Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499 at ¶¶ 269-270 (rel. Aug.

the investment decisions of competitors as they enter local telecommunications markets.[6]

UNE prices and rate structures are set by regulation and therefore UNE competition will not offer the benefits promised by the FCC's market-based approach. Only facilities-based competition can "ensure that goods and services are provided to consumers in the most efficient manner possible."[7]

Moreover, there is no question that facilities-based access competition is in fact developing. As Chairman Kennard recently stated, the top 10 competitive local exchange carriers have installed switches in 132 cities in 33 states and the District of Columbia.[8] TWComm alone has installed 16 switches. The petitioners' complaint that little access competition has developed in the two years since passage of the Telecom Act of 1996 borders on the frivolous.[9] It has understandably taken new

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6 See Access Charge Order at ¶ 263; Id. at ¶ 289 ("Prescribing TSLRIC-based access rates would be the most direct, uniform way of moving those rates to cost. But, precisely because of its directness and uniformity, rate regulation can only be, at best, an imperfect substitute for market forces. . . . A market-based approach to rate regulation should produce for consumers of telecommunications services, a better combination of prices, choices, and innovation than can be achieved through rate prescription").

7 Petitioners and supporting commenters thus mischaracterize the Access Charge Order when they state, as AT&T does for example, that "network element based competition is the primary and nearly exclusive mechanism the Commission expected to generate competition over the next several years." See Comments of AT&T at 5.

8 See "Press Statement of Chairman William E. Kennard on the Second Anniversary of the Telecom Act of 1996," January 30, 1998.

9 See CFA Petition at 5.

entrants, legally prohibited to enter the local market in many states before 1996, some time to reach interconnection agreements, raise capital, build networks and begin to market their services. Moreover, it has been just nine months since the Commission released the rate structure reforms that establish the preconditions for efficient competitive entry for many access services that have been previously effectively sheltered from competition (most of the rules became effective only a month and a half ago).[10] While there is much promising activity, it is simply unreasonable to expect broad results at this early stage.

In any case, as the February 2001 deadline for the submission of cost studies demonstrates, the Commission fully expected that its market-based approach "may take several years to drive costs to competitive levels."[11] The Commission also recognized that "competition is unlikely to develop at the same rate in different locations, and that some services will be subject to increasing competition more rapidly than others."[12] This is of course consistent with the profit-maximizing

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10 Until recently, the transport interconnection charge essentially subsidized prices for incumbent LEC tandem switching and tandem-switched transport. It is therefore no surprise that "no carrier provides competitive tandem switching or tandem-switched transport." Comments of CompTel at 8. It is of course far too early, however, to conclude, as CompTel does (id. at 8), that the gradual elimination of this subsidy flow ordered by the Access Charge Order has failed to establish the preconditions for competitive entry.

11 Access Charge Order at ¶ 45.

12 Id. at ¶ 266.

incentives of new entrants. New entrants can be expected to serve the most profitable, high-priced customers first. This is because during the initial phase of competition there will be a greater opportunity cost associated with serving less profitable customers. As competition develops for serving the most profitable customers, the margins for serving those customers diminishes. Eventually, the relative profitability of serving the lower-priced customers increases and competitors will begin to market services to those customers as well.[13]

Finally, the petitioners blithely ignore the massive undertaking required by any prescriptive approach to interstate access charges. The seemingly endless debate surrounding the selection of forward-looking cost proxy models in the universal service proceeding demonstrates just how difficult it is to resolve this sort of inquiry.[14] The virtual collocation tariff review process is another cautionary tale. The Commission has

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13 See id. at ¶ 266 n.349.

14 The FCC noted somewhat optimistically in the Access Charge Order that the development of cost proxy models for interstate access could take "a year or more to complete." See id. at ¶ 45. Moreover, AT&T is incorrect that the universal service cost proxy models can simply be applied to interstate access. See Comments of AT&T at 23 n. 23. This is because any estimate of cost will necessarily require an allocation of the substantial joint and common costs associated with interstate access service. The virtual collocation tariff review proceedings demonstrate just how contentious and time-consuming such decisions will be. Similarly, CompTel is incorrect that state UNE prices can be used to set access prices, see Comments of CompTel at 8-9, since the price for a *service* will generally include many more joint and common costs than the price for a *network element*. See Local Competition First Report and Order at ¶ 695.

spent more than three years trying to set prices for virtual collocation services, small compared to interstate access as a whole, and it still has not fully resolved the issue. Prescriptive reform would probably also require separations reform as the incumbents would claim that shortfalls in interstate access revenues must be recovered through higher charges for intrastate services.[15] The states, especially high cost states, would likely resist rebalancing. Finally, the incumbent LECs would of course appeal the ultimate FCC orders, thus further delaying resolution of the issue. Such appeals would be pursued for the same reasons and with the same determination as those challenging the FCC's UNE rules.

Once the Commission has settled on prescriptive rate levels, still more time would be needed to phase-in TSLRIC-based rates. As the Commission stated in the Access Charge Order, "[w]ere we to make such a rate prescription, we would consider phasing in rate reductions of that magnitude over a period of years, in order to avoid the rate shock that would accompany such a great rate reduction at one time."[16]

In sum, the CFA petition offers no basis for reassessing the FCC judgment that market forces should be relied upon as the primary vehicle for lowering interstate access charges. It is simply too early to revisit these issues.

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[15] In fact, U S WEST has already begun to make this claim. See Comments of U S WEST at 5.

[16] See Access Charge Order at ¶ 290.

CONCLUSION

The Commission should deny the instant petition for the reasons described above.

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CERTIFICATE OF SERVICE

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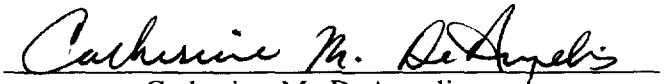

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